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AMERICAN SHORT LINE AND
REGIONAL RAILROAD ASSOCIATION
The Voice of America's Independent Railroads

Alice C. Saylor
Vice President & General Counsel

November 17, 2000
Via Messenger

Vernon A. Williams, Secretary
Surface Transportation Board
1925 K. Street, N.W.
Washington, D.C. 20423-0001

Re: STB Ex Parte No. 582 (Sub-No. 1),
Major Rail Consolidation Procedures

Dear Secretary Williams:

Attached for filing with the Surface Transportation Board are the original and twenty five paper copies of the Comments of the American Short Line and Regional Railroad Association being submitted for filing in the above-captioned proceeding. A copy on diskette is also enclosed.

Please date-stamp the duplicate copy to indicate receipt and return it to the messenger. Thank you.

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Sincerely,

Alice C. Saylor

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Before the
Surface Transportation Board
Washington, D.C.

STB Ex Parte No. 582 (Sub-No. 1),
Major Rail Consolidation Procedures

COMMENTS OF THE AMERICAN SHORT LINE AND REGIONAL RAILROAD ASSOCIATION

The American Short Line and Regional Railroad Association (ASLRRA) is submitting these comments on behalf of its 418 short line and regional railroad members in response to the Notice of Proposed Rulemaking (NPRM) in the above-captioned proceeding (decision served October 3, 2000). The NPRM seeks public comment on the Board's proposed modifications to its regulations at 49 CFR part 1180 governing proposals for major rail consolidations. ASLRRA participated in the earlier stages of this proceeding. ASLRRA President Frank K. Turner testified on March 8, 2000 at the hearing in Ex Parte No. 582, *Public Views on Major Rail Consolidations,* and ASLRRA filed comments on May 16, 2000 in response to the Advance Notice of Proposed Rulemaking (ANPRM) in this Ex Parte No. 582 (Sub-No. 1) proceeding.

ASLRRA is a non-profit trade association incorporated in the District of Columbia. ASLRRA represents the interests of its short line and regional railroad members in legislative and regulatory matters. Short line and regional railroads are an important and growing component of the railroad industry. Today, they operate and maintain 29 percent of the American railroad industry's route mileage (approximately 50,000 miles of track), and account for 9 percent of the rail industry's freight revenue and 11 percent of railroad employment.

ASLRRA and its members applaud the Board for the stated overall objectives of the proposed new merger rules, but urge the Board to revise the draft rules to add specific requirements to accomplish those objectives. If the Board's intent is to raise the bar for applicants, then ASLRRA urges the Board to make the rules more specific in terms of what will be required.

The Board's Proposed Rule

In the NPRM the Board states: "These proposed new rules would substantially increase the burden on applicants to demonstrate that a proposed transaction is in the public interest, requiring them, among other things, to demonstrate that the transaction would enhance competition as an offset to negative impacts resulting from service disruptions and competitive harms likely to be caused by the merger."

This objective is well stated. ASLRRA has no quarrel with what the NPRM says the proposed rules are intended to accomplish. However, ASLRRA has serious concern with what the proposed rules actually do - - in other words, whether the proposed rules as currently drafted will actually accomplish the Board's stated objective.

The proposed rules do not clearly carry through the Board's intent to increase the burden on applicants to enhance competition and offset negative impacts of service disruptions and competitive harms. In ASLRRA's view, the proposed rules are not specific enough about what will be required of applicants in future Class I mergers. There is too much leeway left for the applicants, and not enough precision about what will be required. The Board paints an accurate picture of the issues and problems that confront the railroad industry as it faces the possibility of further major consolidations, but the Board's proposed rules do not go far enough in specifying how these problems should be addressed. ASLRRA urges the Board to put "teeth" in the rules by adding specific minimum conditions that will be required to enhance competition and protect essential services.

The "Short Line and Regional Railroad Bill of Rights"

ASLRRA respectfully suggests that the Board take another look at the "Short Line and Regional Railroad Bill of Rights" conditions proposed in ASLRRA's comments filed on May 16, 2000 in this proceeding. Those conditions specifically address the service and competitive issues that are of critical concern to small railroads. They are

based on what we have learned from past mergers to be the most critical recurring issues. They are designed to safeguard the public interest, which is the touchstone for merger analysis. In its filing, ASLRRA suggested that the new merger rules should include conditions for the benefit of class II and class III railroads, as follows:

> ***(1) Class II and class III railroads that connect to the consolidated carrier have the right to compensation by the consolidated carrier for service failures related to the consolidation. In addition, when the consolidated carrier cannot provide an acceptable level of service post-transaction, connecting class II and class III railroads should be allowed to perform additional services as necessary to provide acceptable service to shippers.***
>
> ***(2) Class II and class III railroads have the right to interchange and routing freedom. Contractual barriers affecting class II and class III railroads that connect with the consolidated carrier that prohibit or disadvantage full interchange rights, competitive routes and/or rates must be immediately removed by the consolidated carrier, and none imposed in the future. The consolidated carrier must maintain competitive joint rates through existing gateways. Also, class II and class III railroads should be free to interchange with all other carriers in a terminal area without pricing or operational disadvantage. Any pricing or operational restrictions which disadvantage connecting class II or class III railroads must be immediately removed by the consolidated carrier, and none imposed in the future.***
>
> ***(3) Class II and class III railroads that connect to the consolidated carrier have the right to competitive and nondiscriminatory rates and pricing. Rates and pricing of the consolidated carrier that do not meet this standard will be promptly corrected by the consolidated carrier upon request by a connecting class II or class III railroad.***
>
> ***(4) Class II and class III railroads that connect to the consolidated carrier have the right to fair and nondiscriminatory car supply. Car supply issues regarding this standard will be promptly addressed by the consolidated carrier upon request by a connecting class II or class III railroad.***
>
> ***<u>Implementation</u>: The Board strongly encourages the consolidated carrier to work out any issues regarding these conditions with its connecting class II and class III carriers in a mutually agreeable fashion without resorting to the Board for interpretation or enforcement. However, if needed, the Board will put in place an expedited and cost-effective remedy process to be initiated by complaint filed with the Board by a connecting class II or class III carrier.***

These conditions are designed to address the critical issues facing small railroads in the merger context. Issues involving service and competition must be dealt with in any future major rail mergers. The Board has acknowledged that the burden on applicants must be substantially increased. The NPRM states that applicants will be required to specify what steps they will take to affirmatively enhance competition and minimize service disruptions. Given that the Board intends to increase the burden on applicants and require applicants to address competitive and service issues, would it not make sense for the new rules to provide more guidance? ASLRRA's suggested Bill of Rights conditions would serve this purpose.

The Rules Should Specify Minimum Conditions for Future Mergers

If the Board specifies minimum acceptable conditions in the rule it would help to clarify what will be required of applicants. Of course, this would simply provide a starting point. Applicants could agree to more than the minimum conditions require. Applicants could also propose variations on the minimum conditions tailored to particular or unique circumstances, or could argue for imposition of less than the minimum conditions if they can convince the Board that the minimum conditions would be inappropriate for their transaction or would be unduly burdensome. Specifying minimum conditions in the rule would still allow a full range of flexibility for the Board to craft appropriate conditions, but the burden would be on applicants to make the case as to why something different than the minimum conditions should be imposed. In effect, the rules would establish a rebuttable presumption in favor of the set of minimum conditions.

This approach would greatly reduce the burden on small railroads, and better accomplish the Board's stated objectives. The minimum conditions might meet the needs of many of the affected small railroads. In that case, there would be no need for numerous small carriers to engage in separate negotiations with the merging carriers covering the same or very similar ground over and over again. This would mean that the concerns of many small railroads would be addressed without the burden and

expense of participating as a party of record in a major merger proceeding, which often involves hiring counsel and considerable time and expense. This can be a very real deterrent for a small company. Minimum conditions in the rule would also address the very real issue of disparity in bargaining power between the merging mega-carriers and their small railroad connections. Minimum conditions would raise the floor from which negotiations begin, making it more likely that private negotiations between the parties could lead to a satisfactory outcome. Adding minimum conditions to the rules would go a long way toward reassuring concerned stakeholders - - not just the small railroads but also shippers, communities and government entities.

The Burden on Small Railroads

If minimum conditions are not added, the Board's merger rules will not effectively address the important issues raised by the small railroads. Requiring hundreds of small railroads that connect with merger applicants to undertake individual negotiations and/or participate in a major regulatory proceeding would be unnecessarily burdensome and expensive. The hundreds of small railroads that will be affected by any future Class I merger simply do not have the resources to put them on an equal footing with the applicants for negotiating, or for litigating before the Board or the courts. The Regulatory Flexibility Act (5 USC §601 et seq.) requires the Board to take into consideration the impact of its rules on small entities, and steps that can be taken to minimize negative effects. The rule as presently drafted will have a significant economic impact on a substantial number of small entities, as explained above. Putting minimum conditions in the rule is an appropriate way for the Board to address the NPRM's Reg-Flex issues.

If the past is prologue, then recent history is not reassuring. The record is not good. The Union Pacific/Southern Pacific merger, and the acquisition of Conrail by CSX and Norfolk Southern, in particular, caused service problems and raised competitive issues that seriously affected many small railroads, shippers and communities. Despite positive predictions in the applications that were filed with the

Board, service problems resulted that were serious enough and lasted long enough to wreak havoc with the rest of the industry. The service problems drove rail business to truck. Small railroads lost business, revenue, and customers (some of which may never come back to rail). These problems were beyond the small railroads' control. They were innocent bystanders that tried to make the best of a bad situation and offered their services to help make things better where they could. The merger-related financial losses the small railroads suffered will never be made up.

With each successive merger, the ante goes up. Rail industry consolidation has proceeded to the point that any further Class I railroad consolidations will have a huge impact. The Board suggests in the NPRM that any further Class I merger proposal would trigger the "final round" of rail industry restructuring. The stakes are very high.

Comments of Other Parties

The appendices to the Board's October 3rd NPRM decision summarize all the comments filed with the Board by interested parties in response to the ANPRM. They reveal a remarkable convergence of opinion. A common thread runs through most of the comments the Board received. Except for the comments of the Class I railroads, almost all of the more than 100 commenting parties consistently urge the Board to require meaningful conditions for any future major rail mergers. The need for service guarantees and conditions to enhance competition and preserve or strengthen competitive options are themes that recur again and again. ASLRRA's Bill of Rights conditions are supported by the vast majority of commenting parties, either by specific reference or in substance.

Comments of Class I Railroads

The comments of the Class I railroads are summarized in Appendix C to the Board's October 3rd decision. Both Burlington Northern Santa Fe's and Canadian National's comments argue that industry competitive issues should be discussed in

another proceeding of industry-wide scope outside of the Class I merger context. ASLRRA has no objection to the Board opening another proceeding for an industry-wide examination of competitive issues. However, those issues must still be addressed in this Ex Parte No. 582 (Sub-No. 1) proceeding. Competitive issues are squarely raised in the merger context. They must be addressed in this proceeding and cannot be delayed for another proceeding at a later time. If an industry-wide proceeding to examine competitive issues is begun later, it can incorporate and build on what is done first in this proceeding in the context of the merger rules.

With respect to competitive issues, several of the Class I railroads comment that the small railroads' competitive concerns are not directly merger related, and the Bill of Rights conditions are not an appropriate response to competitive concerns. Norfolk Southern's comments state that ASLRRA's Bill of Rights conditions concern longstanding commercial disputes that have little or nothing to do with the actual effects of rail mergers, and argue that the conditions would undo freely negotiated deals and deter future line sales. Union Pacific's comments take the position that in general, short line and regional railroad issues are not merger related, and that they are more appropriately the subject of private industry negotiation under the Railroad Industry Agreement framework. Both of these comments miss the mark. Competitive issues are at the heart of the issues that the Board's new merger rules must address. Major mergers do have a major effect on competition and the Board must deal with these issues before approving a major merger application. The public interest requires this.

With regard to service issues, CSX's comments warn that no railroad is so well capitalized that it can afford to offer all of its customers a "business interruption insurance policy" that would cover the full extent of the customers' commercial expectation interest. CSX further argues that the Board does not want to get into the business of handling freight claims. These comments also miss the mark. Merger proponents typically assure the Board in their application that they will plan for and implement the merger carefully and service will not suffer. They should be held to that standard, and be accountable if their promises are not kept. Their small railroad

connections suffer financial losses that are beyond their control. Their shippers do too, of course. This threatens the small railroads' viability and weakens the rail network. Compensation of connecting small railroads for merger related service failures should be required. The Board does not need to get into the business of handling freight claims. Hopefully most claims would not be disputed, and an expedited process could be put in place to handle those that are.

Comments of Small Railroads

Appendix D summarizes the comments filed by small railroads and by ASLRRA. Looking at the small railroads, a dozen small railroads or groups of small railroads filed comments in response to the ANPRM. Most focused on competitive and service issues, and ask the Board to require meaningful conditions. Many support ASLRRA's Bill of Rights conditions expressly. These small railroads consistently emphasized the themes of how real the service and competitive issues are for their businesses, and how unrealistic it would be to rely on negotiation of suitable conditions with the much larger Class I carriers in a merger context.

Comments of Federal Agencies

Government agencies also support imposition of meaningful conditions. The U.S. Department of Agriculture's comments state that merging carriers should be required to reimburse shippers and other railroads for losses due to merger related service disruptions. The Department's comments point out that short line railroads are important to agriculture, and diversion of agricultural goods to truck due to service failures can damage rural road infrastructure.

The U.S. Department of Transportation favors requiring service benchmarks and guarantees of service, including car supply, for class II and class III railroads. The Department supports including paper barriers in the scope of merger review, stating that

they should be removed only to address specific merger issues or on a temporary basis to resolve implementation problems.

Comments of Regional and Local Interests and Shippers

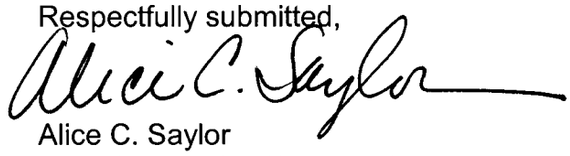
State, regional and local interests weighed in strongly on the side of rules that would specifically enhance competition and ensure service. Several specifically endorsed the ASLRRA Bill of Rights conditions.

The many shippers and shipper groups that commented all urge the Board that now is the time to take meaningful steps to enhance competition and ensure adequate service. Shippers both large and small, representing every part of the country and every type of commodity that moves by rail, asked the Board to make meaningful conditions a part of any future merger approval process.

* * * * *

ASLRRA urges the Board to add specific conditions to the NPRM's draft merger rules. Only in this way will the Board's stated intent of raising the bar for merger approval, enhancing competition and safeguarding service be more than just words. Minimum conditions in the rules would make the process less burdensome and more user friendly for small railroads. ASLRRA's Bill of Rights conditions address the service and competitive issues that will arise in any future Class I merger. ASLRRA urges the Board to add these conditions to its merger rules.

Respectfully submitted,



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Date: November 17, 2000

Certificate of Service

I certify that on this 17th day of November, 2000, I have caused a copy of these Comments of the American Short Line and Regional Railroad Association to be served on all parties of record in STB Ex Parte No. 582 (Sub-No. 1) by first class U.S. mail, postage prepaid.

Alice C. Saylor

Date: November 17, 2000